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JEROME D. GERARD
ACTING EXECUTIVE DIRECTOR

November 19, 2004

Dear Revenue Forecasting Committee Members:

Pursuant to 5 MRSA, § 1710-J, Maine Revenue Services (MRS) is providing the committee with a report on the amount of capital gains and losses realized by taxpayers filing Maine individual income tax returns for tax year 2002.

The information on capital gains and losses realized by individual taxpayers reflect income reported to both MRS and the Internal Revenue Service (IRS) by Maine resident filers. The attached table for individual income tax returns is based solely on Maine residents. MRS has concluded that data on non-resident filers is insufficient to accurately measure the amount of capital gains and losses taxable in Maine.

As reported in Table 1, there were 57,733 individual income tax returns reporting a positive level of capital gains realizations in tax year 2002, totaling \$1,034 million. There were 51,982 returns reporting a capital loss in tax year 2002, totaling \$117.3 million. Net capital gains realizations in tax year 2002 reported by Maine resident filers was \$916.6 million, translating into \$62.7 million in individual income tax revenue.

At the bottom of Table 1 is a short history of net capital gains realizations reported on Maine resident individual income tax returns. The 2002 level of net realizations represents a 17.3 percent decrease over the 2001 tax year. This time series of net realizations demonstrates the remarkable increase in capital gains realized by Maine residents for the 5 year period ending with the 2000 tax year, and the subsequent "crash" in 2001. We estimate that the stock market correction resulted in a \$118 million annual reduction in individual income tax liability by Maine residents.

We have included two graphs that show how the stock market's rapid appreciation and subsequent decline has impacted state income tax revenues. The first graph shows the actual growth in capital gains realizations between 1995 and 2002, the growth in capital gains estimated by the Revenue Forecasting Committee for those tax years, and the current forecast of capital gains realizations by the committee for tax years 2003 through 2005.

The second graph demonstrates how reliant the state had become on capital gains realizations by tax year 2000. MRS estimates that taxes from capital gains represented 17.5 percent of total resident income tax liability in tax year 2000, compared with over 6 percent of total resident income tax liability in tax year 1995. Based on the Revenue Forecasting Committee's forecast, we estimate that taxes on net capital gains will only represent 6.5% of resident income tax liability for the foreseeable future.

If you need any further information, please feel free to contact me.

Sincerely,

Jerome D. Gerard
Acting Executive Director

Capital Gains and Losses Reported on Maine Individual Income Tax Returns, Tax Year 2002 /1

<u>Decile</u>	<u>Expanded</u> <u>Income Range</u>			<u>Returns with Net Capital Gains</u>			<u>Returns with Net Capital Losses</u>			<u>Returns with Capital Gains/Losses</u>		
				<u>Thousands</u>	<u>(Millions of Dollars)</u>		<u>Thousands</u>	<u>(Millions of Dollars)</u>		<u>Thousands</u>	<u>(Millions of Dollars)</u>	
				<u>Returns</u>	<u>Gains</u>	<u>Revenue</u>	<u>Returns</u>	<u>Losses</u>	<u>Revenue</u>	<u>Returns</u>	<u>Gains</u>	<u>Revenue</u>
First & Second	\$0	-	\$8,825	5,176	\$16.2	\$0.1	7,990	(\$18.5)	(\$0.1)	13,166	(\$2.2)	(\$0.0)
Third	\$8,826	-	\$13,120	2,670	\$6.4	\$0.1	2,327	(\$5.1)	(\$0.1)	4,997	\$1.2	\$0.0
Fourth	\$13,121	-	\$18,516	3,970	\$11.9	\$0.3	3,069	(\$6.8)	(\$0.2)	7,039	\$5.1	\$0.1
Fifth	\$18,517	-	\$24,883	4,196	\$13.2	\$0.4	3,410	(\$7.5)	(\$0.2)	7,606	\$5.7	\$0.2
Sixth	\$24,884	-	\$33,046	4,861	\$18.1	\$0.7	3,928	(\$8.6)	(\$0.3)	8,789	\$9.5	\$0.4
Seventh	\$33,047	-	\$43,796	6,027	\$26.1	\$1.2	5,059	(\$10.9)	(\$0.5)	11,086	\$15.3	\$0.7
Eighth	\$43,797	-	\$58,695	7,748	\$41.6	\$2.3	6,097	(\$13.2)	(\$0.7)	13,845	\$28.4	\$1.5
Ninth	\$58,696	-	\$83,291	9,633	\$77.2	\$5.0	8,021	(\$17.5)	(\$1.1)	17,654	\$59.7	\$3.9
<u>Tenth</u>	<u>\$83,292</u>	<u>&</u>	<u>Over</u>	<u>13,452</u>	<u>\$823.1</u>	<u>\$58.0</u>	<u>12,081</u>	<u>(\$29.2)</u>	<u>(\$2.1)</u>	<u>25,533</u>	<u>\$793.9</u>	<u>\$56.0</u>
Total				57,733	\$1,033.9	\$68.0	51,982	(\$117.3)	(\$5.3)	109,715	\$916.6	\$62.7

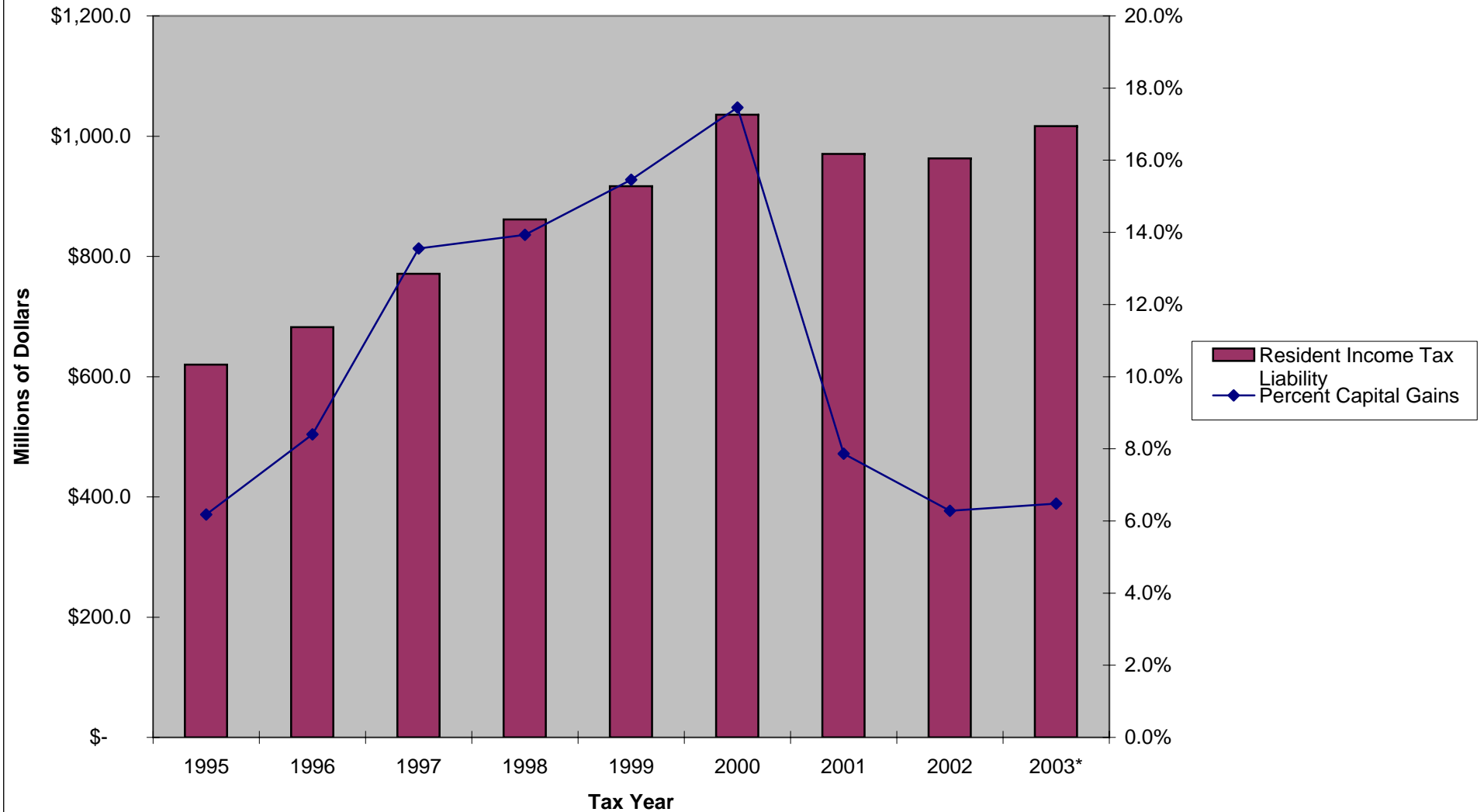
Total Resident Tax Returns filed in Tax Year 2002 = 573,231

Total Resident Tax Liability in Tax Year = \$965.1 Million

1/ Based on Maine Revenue Services' Individual Income Tax Model. Data is from tax returns filed with the Internal Revenue Service and Maine Revenue Services.

	<u>Resident</u> <u>Net Gains</u> <u>(\$ Millions)</u>	<u>% Change</u>
1995	\$551.7	
1996	\$799.7	45.0%
1997	\$1,218.7	52.4%
1998	\$1,551.0	27.3%
1999	\$1,867.2	20.4%
2000	\$2,360.3	26.4%
2001	\$1,108.0	-53.1%
2002	\$916.6	-17.3%

Percentage of Resident Liability Attributable to Net Capital Gains



* Signifies a forecasted value.